IN THE

Supreme Court of the United States

OCTOBER TERM, ~~1950~~ 51

No. ~~584~~ 11

THE UNITED STATES, *Petitioner,*

v.

MARTIN WUNDERLICH, ANN M. WUNDERLICH, MARIE WUNDERLICH, E. MURIELLE WUNDERLICH and THEODORE WUNDERLICH, a Partnership, Trading Under the Name of MARTIN WUNDERLICH COMPANY.

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

INDEX.

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Respondents pray that the petition for a writ of certiorari to review the judgment of the Court of Claims entered in the above-entitled case on June 5, 1950, be denied.

OPINION BELOW.

The opinion of the Court of Claims (R. 159-170) is reported at 117 C. Cls. 92.

JURISDICTION.

The judgment of the Court of Claims was entered on June 5, 1950 (R. 170). A motion for a new trial, filed on August 14, 1950 was denied on October 2, 1950 (R. 171). By an order of the Chief Justice, dated December 26, 1950,

the time for filing a petition for a writ of certiorari was extended to and including March 1, 1951 (R. 174). The jurisdiction of this Court is invoked under 28 U. S. C. 1255.

QUESTIONS PRESENTED.

Article 3 of the standard form government construction authorizes changes in the contract work, requires an "equitable adjustment" in the contract price on account of such changes, and provides for appeal to the head of the department as provided in Article 15 if the contractor and contracting officer cannot agree on the adjustment. Article 15 provides that "all disputes concerning questions of fact arising under this contract shall be decided by the contracting officer subject to written appeal * * * to the head of the department * * * whose decision shall be final and conclusive upon the parties thereto". In this case a change was ordered, the contracting officer made an adjustment which was appealed because of the gross inadequacy of the amount allowed for rental of respondents' equipment and for the cost of its repair and maintenance, and the head of the department affirmed the decision of the contracting officer. In their petition in the Court of Claims, respondents did not allege bad faith, arbitrariness, or error so gross as to imply bad faith, but did allege that the reasonable amount due on a cost plus 10 percent basis was $181,721.10 instead of the $44,208.85 allowed (but never paid) by the contracting officer and the head of the department. The Government's trial attorney was also aware from the outset that the only issue in this claim concerned the fairness of the administrative allowance for equipment. The Court of Claims found that the methods used by the contracting officer and the head of the department in computing the hourly rental rates for equipment and the cost of its repair and maintenance were arbitrary and capricious and that the results obtained thereby were grossly erroneous. It then set aside the administrative adjustment on the ground that it was arbitrary and capricious.

The questions presented are:

1. Whether the decision of the Court of Claims setting aside the administrative adjustment because it was arbitrary and capricious is in accordance with the principles of judicial review laid down by this Court.

2. Whether the finding of the Court of Claims that the administrative methods of computing equipment rental and the cost of its maintenance and repair were arbitrary and capricious is supported by the evidence.[1]

CONTRACT PROVISIONS INVOLVED.

Pertinent portions of the contract and specifications are set forth in the Appendix, *infra*.

STATEMENT.[2]

This case grows out of the performance of a contract to build a dam for the Government acting through the Bureau of Reclamation. Respondents received notice to proceed on April 18, 1938 and completed the work satisfactorily in October, 1941 (R. 67). Various claims arose during the performance of the work, some of which became the subject of a suit in the court below (R. 76-77). The petition for a writ of certiorari is directed only to Claim No. 17. This claim concerns the amount of an adjustment made by the contracting officer and approved by the head of the department pursuant to a change order. The dispute centers upon the amount allowed in such adjustment for the use of respondents' equipment and for its repair and maintenance.

a. **Background of the order for changes and the adjustment thereunder.**—The principle feature of the contract

[1] Petitioner asserts that one of the questions presented is whether the holding of the Court below that the determination of an equitable adjustment is a question of law conflicts with *United States* v. *Callahan Walker Co.*, 317 U.S. 56. As shown, *infra*, pp. 9-10, the Court below did not so hold.

[2] Because petitioner's Statement fails to set forth certain facts pertinent to the issues here presented and draws conclusions with which respondents cannot agree a Statement is included in this brief.

work was the rolled earth-fill dam, consisting of an impervious core grading to more pervious materials upstream and downstream from the core. The upstream slope of this fill was faced with rock riprap and on the face of the downstream slope was a cobble fill (R. 67-68). The materials for the earth portion of the fill were to come from earth borrow pits. They were also to come from the various items of required excavation and from cobble borrow pit excavation after being separated into material 2½ inches or more in diameter and material less than 2½ inches in diameter. The materials for the cobble fill portion of the dam were to consist of the plus 2½-inch material, after separation, taken from the various items of required excavation and from cobble borrow pits. No separation was specified for materials taken from earth borrow pits (R. 50, 51, 52, 54-56, 61). The contract drawings showed two areas upstream from the dam designated as earth embankment borrow pit areas, the one on the right side of the river later being designated as Borrow Pit No. 1, and the one on the left side as Borrow Pit No. 2. The contract drawings also showed a cobble borrow pit area downstream from the dam on the left side of the river (R. 68, 113). The contract unit price for excavating and hauling earth borrow (Item 14) was 23 cents per cubic yard, and for excavating, separating and hauling cobble borrow (Item 16) was 35 cents per cubic yard (R. 31).

In 1938 respondents excavated impervious materials in Borrow Pit No. 2, and exposed underlying materials containing a high percentage of cobbles. No further excavation was performed in Borrow Pit No. 2 until the late fall of 1939, earth borrow materials meanwhile being obtained from Borrow Pit No. 1. In the late fall of 1939 respondents were directed to resume excavation in Borrow Pit No. 2 and performed such work under protest at the payment of the contract unit price for earth borrow because of the high cobble content (R. 114-115). After the winter lay-off, respondents were directed to resume excavation in Borrow

Pit No. 2 and in extensions of that borrow pit upstream and farther away from the dam, and had to resort to expensive separation processes because of the cobbles encountered. Work in Borrow Pit No. 2 was completed in November, 1940 (R. 115-117). No cobbles were ever taken from the area designated on the contract drawings as a cobble borrow pit area (R. 113).

During 1940 respondents both in writing and at conferences with the contracting officer, objected to payment of the earth borrow price of 23 cents for materials taken from Borrow Pit No. 2 because of their high cobble content (R. 115-120). Finally, by Order for Changes No. 3, dated August 31, 1940, the contracting officer directed respondents to obtain cobbles for cobble fill from "earth embankment borrow" instead of obtaining them from the cobble borrow pit area shown on the contract drawings, the claim for adjustment by reason of the change to be submitted at a later date (R. 120-121).

b. **The adjustment under Order for Changes No. 3.**—Respondents submitted and the contracting officer considered the claim for adjustment under Order for Changes No. 3 on the basis of the cost of excavating, separating and hauling materials from Borrow Pit No. 2 to the embankment, plus 10 percent for overhead and profit. With exceptions now immaterial he found that respondents' figures for hours of labor and rates of pay, for hours of use of equipment, and for the cost of materials were correct (R. 121). However, he found that respondents' hourly rates for the use and maintenance of equipment were excessive and allowed for these items much less than claimed by respondents (R. 122).

The hourly rates used by the contracting officer to reimburse respondents for the use or rental of their equipment were derived from monthly rates appearing in the Bureau of Reclamation's equipment rental schedule (Pltf. Ex. 17-C), which in turn is based upon and similar to the Asso-

ciated General Contractors' equipment schedule (Pltf. Ex. 17-B). In each the monthly rates are designed to reimburse the contractor for the annual expense of interest on invested capital, depreciation, insurance, taxes, storage, major repairs, general overhauling and painting and equipment overhead. They cover the use of equipment only and do not cover field repairs and maintenance which are paid for separately. These monthly rates are obtained by dividing the total average annual expense for such items by the average number of working months (in most cases eight) that the equipment is used. In each schedule the monthly rates are based upon one-shift operation. Where the equipment is on two-shift operation, one-half of the first shift rate is added for the second shift (R.125-127). The Associated General Contractors' monthly equipment rates are paid for the entire calendar period that the equipment is assigned to the job without deduction for the time that the equipment is idle (Pltf. Ex. 17-B, pp. 2-3). Likewise, as respondents' own witnesses admitted (Tr. 1665-1666, 1689-1691),[3] when the Bureau uses its monthly rates the contractor is paid the full monthly rate even though the equipment may be idle part of the time due to weather, holidays or repairs.

In the adjustment under Order for Changes No. 3, monthly rates could not be applied because respondents' equipment was constantly shifting back and forth between work in Borrow Pit No. 2 and other items of the work. Records were kept of the hours of actual operation and hourly rates therefore had to be used in the adjustment (R. 127). There is no dispute as to the fairness of the Bureau's monthly rates but only as to the method by which they were reduced to hourly rates for application to hours of actual operation (R. 125). What the contracting officer did in the case of equipment which was only on one-shift

[3] The citation "Tr." refers to the transcript of testimony which was sent up by the Court of Claims, together with certain exhibits and other portions of the record in the case (R. 171-174).

operation was to divide the monthly rate by 30 to get a daily rate, and divided the daily rate by 8 to get an hourly rate, and applied such hourly rate to hours of actual operation. This method obviously failed to reimburse respondents for the idle time which is customarily paid for in the Bureau's monthly rate. Most of the equipment was in actual operation on the first shift about 80% of the working season and on the second shift about 80% of the first shift use. For equipment so used the contracting officer divided the monthly rate by 30 to get a first shift rate, added one-half for the second shift, and divided the total by 16 hours to obtain the hourly rate to be applied to hours of actual operation (R. 127, Deft. Ex. 17-W; Tr. 1660, 1664-1665, 1678). Thus, in addition to failing to reimburse respondents for the idle time customarily paid for in the monthly rate, the contracting officer's hourly rates gave equal weight to the lower second shift rate although the equipment was used much more on first shift operations. As found by the Court below, this method of computing hourly rental rates for equipment was arbitrary and capricious, and the result arrived at by this method was grossly erroneous (R. 170-171).

In addition to the hourly rental rates the contracting officer also used hourly rates for repair and maintenance of the equipment. These rates were not based upon respondents' actual costs. They were arrived at by the use of arbitrary percentages and represented only a small fraction of respondents' actual costs for repairs and maintenance (R. 129-130). As found by the Court below, the method used by the contracting officer in determining these rates was arbitrary and capricious and the result obtained thereby was grossly erroneous (R. 171).

Basing his award for use of respondents' equipment on rental and maintenance allowances computed in the manner just described, the contracting officer concluded that respondents were entitled to an equitable adjustment of $40,400.15 in addition to the $194,784.93 already paid for

the excavation in Borrow Pit No. 2 during 1940 (Pltf. Ex. C, p. 48). Applied to the yardage excavated in 1940, this represented a rate of $0.0477 per cubic yard in additional compensation which the contracting officer then allowed for the 79,847 cubic yards excavated in Borrow Pit No. 2 during 1939 (*Id.* p. 50; R. 122). Adding the $3,808.70 so determined, the contracting officer awarded respondents a total of $44,208.85 in his decision of December 29, 1942 (R. 122, 125).

Petitioner appealed to the Secretary of Interior from the decision of the contracting officer, pointing out, among other things, that in reducing the monthly equipment rates to hourly rates the contracting officer deprived respondents of the allowance for idle time which is included in the monthly rates (R. 125, Pl. Ex. D, pp. 56-57). On appeal the Assistant Secretary of the Interior affirmed the allowance of the contracting officer in a decision which did not even discuss the fact that the method used by the contracting officer in reducing the monthly equipment rates to hourly equipment rates to be applied to hours of actual operation failed to reimburse respondents for the idle time paid for in the monthly rates (R. 125, Pltf. Ex. E, pp. 14-16).

c. **The decision of the Court of Claims.**—The Court below found that the methods used by the contracting officer and the head of the department in computing hourly rental rates for equipment and the cost of its repair and maintenance were arbitrary and capricious and that the results arrived at thereby were grossly erroneous (R. 127-130, 170-171). The Court of Claims set aside the decision of the contracting officer and head of the department because of the arbitrary and capricious administrative treatment of respondents' claim (R. 168-169). Using hourly rental rates which made an allowance for the idle time paid for under the monthly rates, and using rates for repair and maintenance of equipment based upon respondents' actual costs, the Court of Claims awarded respondents $155,748.44 in lieu of the $44,208.45 allowed (but never paid) by the contract-

ing officer and the head of the department on this claim (R. 127-132, R. 169).

REASONS FOR DENYING THE WRIT.

1. Petitioner asserts that the Court of Claims held that the administrative adjustment in Claim No. 17 involved a disputed question of law which was not covered by Article 15 relating only to disputed questions of fact. Thus, says petitioner, this holding conflicts with *United States* v. *Callahan Walker Construction Co.*, 317 U. S. 56. Respondents never made any such contention nor did the Court of Claims so hold as a reading of its decision will demonstrate. Petitioner relies on certain language of the Court below in the introductory part of its opinion (R. 161-166). There the Court was considering the question of the finality of the contracting officer's decision in situations where respondents were directed to perform a certain work which they contended was outside the requirements of the contract documents and requested written instructions which the Government failed to give. Distinguishing the provision of the specifications involved in *United States* v. *Moorman*, 338 U. S. 457, the Court of Claims held that paragraph 14 of the specifications[4] in the present case did not purport to make the decision of the contracting officer or head of the department final on questions of interpretation of the requirements of the contract documents where the con-

[4] Paragraph 14 of the specifications (R. 72) provides:

14. *Protests.*—If the contractor considers any work demanded of him to be outside the requirements of the contract, or considers any record or ruling of the contracting officer or of the inspectors to be unfair, he shall immediately upon such work being demanded or such record or ruling being made, ask for written instructions or decision, whereupon he shall proceed without delay to perform the work or to conform to the record or ruling, and, within 10 days after date of receipt of the written instructions or decision, he shall file a written protest with the contracting officer, stating clearly and in detail the basis of his objections. Except for such protests or objections as are made of record in the manner herein specified and within the time limit stated, the records, rulings, instructions, or decisions of the contracting officer shall be final and conclusive. Instructions and/or decisions of the contracting officer contained in letters transmitting drawings to the contractors shall be considered as written instructions or decisions subject to protest or objections as herein provided.

tractor had followed the prescribed avenue of administrative relief as far as possible to do so. The Court below then went on to hold that the failure of paragraph 14 to make administrative decisions final on disputes as to the interpretation of the contract requirements was not cured by Article 15 which related only to questions of fact and not to questions of law such as interpretation of the contract documents.

The situation to which this part of the Court's opinion was directed applied in nearly every claim except Claim No. 17. In Claim No. 17, however, there was no refusal by the Government to give written instructions nor is there any dispute over interpretation of the requirements of the contract documents. On the contrary, by issuing Order for Changes No. 3, defendant admitted that the work required in this claim was a change in the contract requirements. In that portion of the opinion dealing specifically with Claim No. 17 (R. 167-169) the Court pointed out that the dispute in this claim was as to the amount of the actual cost of the work, and does not even suggest that any question of interpretation of the specifications is involved. It set aside the administrative adjustment because of the arbitrary and capricious treatment of this claim. It is, therefore, clear that the Court below did not consider or hold that the dispute in Claim No. 17 involved a question of law, i.e., an interpretation of the contract documents. Thus, its decision is not in conflict with *United States* v. *Callahan Walker Construction Co., supra.*

2. The holding of the Court of Claims that the administrative adjustment should be set aside because of the arbitrary and capricious methods used by the contracting officer and head of the department in computing equipment rental and the cost and maintenance of equipment, is not in conflict with the principles of judicial review laid down by this Court. This Court has laid down the rule that administrative decisions under a contract may be set aside where they are the result of fraud, failure to exercise an

honest judgment, bad faith, or so grossly erroneous as to imply bad faith. *Kihlberg* v. *United States*, 97 U. S. 398, 402; *Sweeney* v. *United States*, 109 U. S. 618, 620. In later cases this Court, in explaining the rule, stated that the administrative officer making the decision must act, not arbitrarily or capriciously, but candidly and reasonably, and with due regard to the rights of both parties. *Ripley* v. *United States*, 223 U. S. 695, 701-702; *Saalfield* v. *United States*, 246 U. S. 610, 613. In the present case the Court below found that the methods used by the administrative officer in computing equipment rental and the cost of its repair and maintenance were arbitrary and capricious and the results obtained thereby were grossly erroneous, and held that the administrative determination should be set aside because of the abritrary and capricious administrative treatment of respondents' claim. It is thus clear that its decision is in accordance with the principles of judicial review laid down in the cases decided by this Court.

No case cited by petitioner holds that an administrative decision which is arbitrary and capricious may not be set aside merely because it is not so characterized in the pleadings. As a matter of fact the contrary appears from the decision of this Court in *United States* v. *Smith*, 256 U. S. 11. There an excavation contract described the material to be removed as consisting of "clay, sand, gravel and boulders" and made the decision of the Government engineer final on questions of quantity and quality. He ordered the contractor to remove bed rock arbitrarily classifying it as clay, gravel, sand and boulders. Despite the Government's contention that the contractor had not pleaded bad faith on the part of the Government officer, this Court refused to follow his classification of the materials and allowed recovery by the contractor for breach of warranty. In *Ripley* v. *United States*, 223 U. S. 695, this Court affirmed a decision of the Court of Claims setting aside an administrative determination which was grossly erroneous and an act of bad faith. Yet the pleadings in that case show

that neither gross error nor bad faith were alleged. Moreover, in the present case it is clear that the Government trial attorney was fully aware that the good faith of the administrative officer was in issue. The petition itself alleged that the reasonable amount due respondents on a cost plus 10% basis was $181,721.10, instead of the $44,208.85 allowed, but never paid, by the contracting officer and the head of the department (R. 10); in other words, that on a cost plus 10% basis there was reasonably due them more than four times the amount allowed. The Government trial attorney, early in his cross-examination, inquired:

> 657XQ. Isn't it a fact that the only controversy now between the parties is as to the fairness of the so-called rental rate? (Tr. 532. See also Tr. 268.)

At no point did he ever object to the materiality or relevancy of respondents' evidence attacking the administrative methods used in arriving at the allowance for equipment, or claim that he was misled in the preparation of his defense. Under these circumstances it is clear that an express allegation of bad faith, or arbitrary and capricious conduct, or failure to exercise an honest judgment, or gross error, was not necessary in order to set aside the administrative determination.

3. The finding by the Court of Claims that the methods used by the contracting officer and head of the department in computing equipment rental rates and the cost of equipment repair and maintenance were arbitrary and capricious and that the results obtained thereby were grossly erroneous is fully supported by the evidence, including that of petitioner's own witnesses. Here the hourly rental rates used by the contracting officer and the head of the department were computed by taking 1/30 of the Bureau's monthly rates to get a daily first shift rate, one-half of the first shift rate was added for the second shift rate, and the total of the two shift rates was divided by 16 hours to obtain an hourly rental rate (Pltf. Ex. 17, pp. 70-77; Tr. 864-866; Tr.

1660, 1664; Deft. Ex. 17-W, Tr. 1678-1680). As admitted by the subordinates in the contracting officer's office who prepared these hourly rates, the Bureau's own monthly rates are paid for the full period that the equipment is assigned to the job without deduction for idle time due to such factors as holidays, weather and repairs (Tr. 1665-1666; Tr. 1686, 1690-1691. See also testimony of respondents' witness Leonard, Tr. 861-863, 866). The hours to which the hourly rates were to be applied were hours of actual operation as the contracting officer had been advised by the Bureau's field office (Deft. Ex. Q). It is obvious, as appears from respondents' testimony (Tr. 866-867) that hourly rental rates derived from the Bureau's monthly rates in the manner followed by the contracting officer do not, when applied to hours of actual operation, make any allowance whatsoever for the idle time which is paid for when the Bureau's monthly rates are used. None of respondents' witnesses ever attempted to deny this fact. On the contrary, respondents' field engineer admitted that such hourly rates made no allowance for idle time (Tr. 1718). Applied to hours of actual operation such hourly rates could never, because of time lost on account of weather, repairs, etc., yield the amount due under the Bureau's monthly rates which everyone agrees are fair and reasonable. In their appeal to the head of the department, respondents protested that the contracting officer's hourly rates took no account of the idle time paid for under the monthly rates (Pltf. Ex. D, pp. 56-57). In his decision on appeal, however, the head of the department never even referred to this vital defect (Pltf. Ex. E, pp. 14-16). Moreover, as stated *supra*, page 7, these hourly rates not only failed to allow for idle time but were grossly unfair for the further reason that they were derived by giving equal weight to both the daily first shift rate and the daily second shift rate (which was one-half the first shift rate) even though the equipment was used much less time on second shift operations than on first shift. In view of the

above, the conclusion is inescapable that the administrative method used in arriving at the hourly rental rates—a method which none of respondents' witnesses even attempted to justify—was not an honest attempt to act with due regard to the rights of both parties, but was, as the Court of Claims found, arbitrary and capricious.

In its brief (pp. 21-22) petitioner seeks to give some justification for the failure of its hourly rates to make any allowance whatsoever for idle time by asserting that the equipment was used not only in Borrow Pit No. 2 but also on other items for which respondents were paid at contract unit prices which presumably reimbursed them for rental of equipment, including idle time, and that by applying its hourly rates to hours of actual operation in Borrow Pit No. 2, the Bureau avoided a possible duplication of payment for idle time. There is no merit to this contention nor a word of testimony to support it. Whether the contract unit prices for work other than that involved in Borrow Pit No. 2 made too little or too much allowance for equipment rental is not shown nor is it material or relevant. For the work in Borrow Pit No. 2 respondents are entitled to a reasonable allowance for the use of their equipment, including a rental which would reimburse them for a fair share of the idle time which is customarily paid for in the rental of equipment. The Court below has made such an allowance by dividing the total rental which would be due respondents for the 1940 working season under the Bureau's monthly rates by the total hours it could normally be operated, taking into account idle time, on all items of work during the same season. The hourly rate thus computed was then multiplied by hours of actual operation in Borrow Pit No. 2 to obtain the rental attributable to work in Borrow Pit No. 2 (R. 127-129). This method avoids any duplication of payment for idle time by arriving at an hourly rate which is fair and reasonable for all hours of operation on the job and applying it only to hours of actual operation in Borrow Pit No. 2. The hourly rates

used by the contracting officer and head of the department, on the other hand, make no allowance whatsoever for idle time. For example, the screening plant was used only on work on Borrow Pit No. 2 during 1940 (R. 116-117); yet the contracting officer and head of the department did not use the monthly rate but used an hourly rate which made no allowance for idle time when applied to hours of actual operation (Deft. Ex. 17-W).

Neither can petitioner justify its hourly rental rates by asserting that the Associated General Contractors' monthly rental rates, upon which the Bureau's monthly rates are based, are merely a guide, and are subject to change in the light of experience. There is not a word of testimony, even after petitioner's auditors inspected respondents' cost records, to suggest that the Bureau's monthly rates were not fair and reasonable in this case. Neither party has ever questioned the fairness of such monthly rates. The only dispute is as to the method of reducing them to hourly rates to be applied to hours of actual operation.

As to the hourly repair and maintenance rates used by the contracting officer and head of the department, the Government employee who prepared these rates admitted that they were not based upon costs on this job (Tr. 1672-1674, 1691-1692), even though paragraph 8 of the specifications (Appendix, *infra*, p. 19) gives the contracting officer complete access to all data of the contractor needed to determine cost. While this witness stated that these hourly rates were based upon the experience of the Bureau and certain other Federal and State agencies (Tr. 1679-1680), he was unable to say how he arrived at the hourly rates used in the adjustment (Tr. 1688). He was requested to furnish to the Court the data he was supposed to have considered in arriving at such hourly rates (Tr. 1688-1689), but never did so nor accounted for his failure to do so. As a matter of fact, Defendant's Exhibit 17-W, which this witness prepared at the time the claim for adjustment was under consideration (Tr. 1674-1675) shows on its face that

these hourly rates did not purport to be based on costs on any job but were mostly arbitrary assumed percentages.

Against these rates are respondents' hourly rates computed by dividing the actual cost for repairs and maintenance for each type of equipment during the 1940 working season by the total hours it worked on all items of work, including Borrow Pit No. 2, during the same season, all these figures being taken from respondents' cost records for the present job (Pltf. Ex. 17-D; Tr. 809-816). There is no real dispute as to the accuracy of such costs or hours, since petitioner, during the trial, sent its auditor to respondents' field office to check these costs but never even called him as a witness (Tr. 2442). The hourly repair and maintenance costs found by the Court of Claims were based upon petitioner's actual costs on the present job, and demonstrated that the amounts allowed for repair and maintenance hourly rates by the contracting officer were only a small fraction of the actual costs experienced (R. 129-130). In view of the above it is clear that the evidence fully supports the finding of the Court of Claims that the method used by the contracting officer and the head of the department in determining the cost of maintenance and repair was arbitrary and capricious and that the result obtained thereby was grossly erroneous.

4. No important questions of law or of public interest are presented by this case. As stated before it was decided by the Court below in accordance with the principles laid down in the decisions of this Court. The case merely presents certain factual questions relating to reimbursement of equipment which are peculiar to this case; have not, to respondents' knowledge, arisen in other cases; and are not likely to do so in the future.

CONCLUSION.

The decision below is in accordance with the decisions of this Court and raises no new important questions of law or of public interest. It is, therefore, respectfully submitted that the petition for a writ of certiorari should be denied.

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JOHN W. GASKINS,
Attorneys for Respondents.

April, 1951.

APPENDIX.

Article 3 of the contract provides:

Changes.—The contracting officer may at any time, by a written order, and without notice to the sureties, make changes in the drawings and/or specifications of this contract and within the general scope thereof. If such changes cause an increase or decrease in the amount due under this contract, or in the time required for its performance, an equitable adjustment shall be made and the contract shall be modified in writing accordingly. No change involving an estimated increase or decrease of more than Five Hundred Dollars shall be ordered unless approved in writing by the head of the department or his duly authorized representative. Any claim for adjustment under this article must be asserted within 10 days from the date the change is ordered: *Provided, however*, That the contracting officer, if he determines that the facts justify such action, may receive and consider, with the approval of the head of the department or his duly authorized representative, adjust any such claim asserted at any time prior to the date of final settlement of the contract. If the parties fail to agree upon the adjustment to be made the dispute shall be determined as provided in article 15 hereof. But nothing provided in this article shall excuse the contractor from proceeding with the prosecution of the work so changed.

Article 15 of the contract provides:

Disputes.—Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the contracting officer subject to written appeal by the contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties thereto. In the meantime the contractor shall diligently proceed with the work as directed.

Paragraph 8 of the specifications provides:

8. *Data to be furnished by contractor.*—The contracting officer, through his authorized agents, shall have access to all pay rolls, records of personnel, invoices of materials, and any and all other data relevant to the performance of the contract or necessary to determine its cost, and the contractor shall furnish at the end of each month an itemized statement in a form satisfactory to the contracting officer of the cost of all work under the contract.

the Government would be the financial loser since substantial amounts would have to be included in all bids to safeguard against arbitrary and capricious action.

B. *An express allegation of fraud or bad faith is not necessary.*—In its brief (pp. 16-19) the Government asserts that the contractor did not allege that the department head's decision was fraudulent, or made in bad faith, or so grossly erroneous as to imply bad faith; that proofs were not directed to the single issue of bad faith and that the Government never had any occasion to defend itself against a charge of fraud or bad faith. Relying on certain decisions of this Court, petitioner then apparently contends that in the absence of such allegations the Court of Claims should not have set aside the departmental decision.

Petitioner submits that the Government was not misled by any lack of an express allegation of bad faith. The petition alleged that the reasonable amount due the contractor on a cost plus 10 percent basis was $181,721.10, instead of the $44,208.85 allowed, but never paid, by the contracting officer and the head of the department (R. 10). An allegation that the cost reasonably due the contractor was more than four times the amount allowed should have put the Government on notice that the good faith of the contracting officer and head of the department were in issue. That it actually did so is shown by the fact that early in his cross-examination the Government trial attorney inquired:

> XQ. 657. Isn't it a fact that the only controversy now between the parties is as to the fairness of the so-called rental rate.
>
> A. Yes, I understand that. (See p. 56 of Appendix C to Brief for the United States).[7]

[7] In its brief (Footnote 11, pp. 18-19), the Government asserts that the issue of the fairness of a rate is at opposite poles with the issue of the honesty of the person who is charged with deciding what is a fair rate. Certainly the question of the fairness of the rate involves the question whether the department head acted "reasonably and with due regard to the rights of both the contracting parties". See *Ripley* v. *United States*, 223 U. S. 695, 702.

At no point did the Government trial attorney object to the materiality or relevancy of respondents' evidence attacking the administrative methods used in arriving at the contracting officer's and the department head's allowance for equipment. Moreover, the Government itself introduced inter-office memoranda between the department head or the contracting officer and their subordinates showing the information that was submitted by the subordinates to aid their superiors to arrive at their decisions (Defts. Exs. K, Q, T, 17-E, 17-U, 17-V, 17-X). The statements in these memoranda, being hearsay, obviously were not competent proof of the facts stated therein. They could have been introduced for no other purpose than to show what factors the contracting officer and head of the department took into account in arriving at their decisions and thus to attempt to show that such decisions were made in good faith.

In view of all of the above it is clear that the Government was well aware that the good faith of the decisions of the contracting officer and department head were being challenged, and that defendant was not perjudiced by lack of any express allegation of bad faith or arbitrariness and capriciousness. Under these circumstances the petitioner should not now be permitted to assert that the administrative decision may not be set aside for lack of such an allegation. As stated by this Court in *District of Columbia* v. *Barnes*, 197 U. S. 146, 154:

> "The Court of Claims is not bound by special rules of pleading. The main purpose is to arrive at and adjudicate the justice of alleged claims against the United States. * * *"

It has long been the rule in the Court of Claims that where errors in the pleading have not misled the opposite party, the pleading may be amended to conform to the proof. *Thomas* v. *United States*, 15 C. Cls. 335, 343. See also *Clark* v. *United States*, 95 U. S. 539, 543, permitting re-

covery upon the basis of *quantum meruit* although the petition was drawn upon the theory of breach of an express contract.

None of the decisions of this Court referred to by the Government holds that the absence of an allegation of bad faith precludes the setting aside of a contracting officer's or department head's decision where there has been no demurrer to the allegation and the proof itself shows bad faith or arbitrary and capricious conduct. In *Kihlberg* v. *United States*, 97 U. S. 398, 401, the Court observed that "There is neither allegation nor proof of fraud or bad faith * * *", but then went ahead and itself considered the question in dispute, stating that the difference between the distances found by the Government officer and the distances by airline or by the road usually traveled were not so material as to justify the inference that he did not act with an honest purpose to carry out the real intention of the parties. Likewise, in *United States* v. *Gleason*, 175 U. S. 588, 607, 608, this Court, although pointing out that the judgment by the Government engineer could only be revised upon allegation and proof of bad faith, or of mistake or negligence so gross as to justify an inference of bad faith, nevertheless proceeded to examine the evidence and the findings of the Court below to ascertain if there was bad faith. In *Sweeney v. United States;* 109 U. S. 618, fraud was alleged but not proved and the Court of Claims refused to hear evidence or make findings that the work was completed in accordance with the contract requirements. The decision of the Court of Claims was then affirmed by this Court on the authority of the *Kihlberg* case. In *Martinsburg & Potomac R. R. Co.* v. *March*, 114 U. S. 549, the trial court overruled a demurrer to a declaration for failure to allege fraud or bad faith and this Court held that the demurrer should have been sustained. In the present case, however, the Government did not demur and proof was taken under circumstances which, as stated *supra*, clearly show that the Government's trial attorney was aware that

the good faith of the departmental decisions was in issue.

Petitioner also cites two decisions of the United States Court of Appeals, Ninth Circuit. In *Lindsay* v. *United States*, 181 F. 2d. 582 (C. A. 9) the opinion does not show whether bad faith was alleged. It does show, however, that the Court reviewed the evidence as to the amount sought by the contractor and the amount allowed by the department head, was convinced that the proof did not support the amount claimed, and affirmed the decision of the trial court that there was no such discrepancy between the amount sought and the amount allowed as to indicate "corruption or a partisan bias", and that the Government officers did not act so inequitably as to justify the Court in setting aside their decision. In *United States* v. *Foster Transfer Co.*, 183 F. 2d. 494 (C. A. 9) the trial court tried the case under pleadings which framed the issue whether the Government representative had good and sufficient cause to cancel the contract, and held that it did have such cause. The Court of Appeals, pointed out that the proof clearly would not support an allegation of fraud or gross mistake even if made, and held that while the receipt of evidence on the issue of performance was a futility neither side was damaged thereby. In the present case, however, the proof does show the arbitrary and capricious character of the administrative decisions, and was received under circumstances which show that the Government trial attorney was aware that the good faith of the Government officers was in issue.

On the other hand, in *Ripley* v. *United States*, 223 U. S. 695, this Court affirmed a decision of the Court of Claims setting aside a determination found to be grossly erroneous and an act of bad faith; yet the pleadings in that case show that neither gross error or bad faith was alleged. In its brief (footnote 11, p. 18) defendant points out that the case had previously been remanded to the Court of Claims for explicit findings as to whether the Government officer acted in good or bad faith (220 U. S. 491, 496; 222 U. S. 144, 148),

and asserts that it cannot be assumed that this Court contemplated findings of this precise character without the production of evidence directed to this particular issue. However, there is nothing in these two opinions to indicate that the Court of Claims was to take further evidence, and, as a matter of fact, an examination of that Court's docket (C. Cls. No. 28555) shows that no further evidence was taken.

The Court's attention is also directed to *United States* v. *Smith*, 256 U. S. 11, where an excavation contract described the material to be removed as consisting of "clay, sand, gravel and boulders", and made the decision of the Government engineer final on questions of quantity and quality. He ordered the contractor to remove bed rock without increase in the contract price, arbitrarily classifying it as clay, gravel, sand and boulders. Despite the Government's contention that the petition did not allege bad faith, this Court refused to follow his classification and allowed recovery for breach of warranty. In its brief (footnote 11, R. 18) petitioner asserts that in the *Smith* case it did not appear that any provision for departmental decision was squarely applicable to the dispute in question, and that the Court obviously did not regard the dispute as within any such provision. This position is certainly contrary to the position taken by the Government in the *Smith* case. Moreover, it is not seen how the Court could have held that there was a breach of warranty without setting aside the Government engineer's determination that the material in question was clay, gravel, sand and boulders rather than bed rock. Such questions would certainly come within the provision making the Government engineer's decision final as to quality and quantity.

Lastly, petitioner appears to argue that proofs should have been directed to the single issue of bad faith or error so gross as to imply bad faith. In cases of this kind, however, such questions are necessarily so inter-related with the merits of the dispute that, as a practical matter, it is ex-

tremely difficult, if not impossible, to separate the two. In this connection it should be remembered that it has long been the practice in the Court of Claims to try the case before a Commissioner, who hears the evidence and makes findings of fact, but does not make findings or recommendations as to liability. Under this practice the Court itself then determines the legal consequences of the facts, and, if it determines that the decision of the Government officer should be set aside, it then awards damages to the plaintiff upon the basis of the Commissioner's report and the proof previously taken in the case. Respondents are not aware of a single case under this practice where the Government has taken the position that proof should be limited to the single issue of good faith.

C. *The proof in the case shows that the departmental decisions were not made in good faith.*—As shown *supra*, pp. 7-12, the decision of the Court below, setting aside the department head's decision because of the arbitrary and capricious methods of computation used by him, comes within the principles of judicial review laid down by this Court. However, even if this Court should hold that the Court below must expressly find that the decision was made in bad faith, or was so grossly erroneous or negligent as necessarily to imply bad faith, or was the result of a failure to exercise an honest judgment, respondents submit that the proof supports such a finding, and that the case should therefore be remanded with instructions for a more explicit finding on the question of good faith.

The undisputed proof in this case shows the following:

The Associated General Contractor's schedule sets forth monthly rates for equipment for use on one-shift operation and provides that such monthly rates are not subject to deductions for idle time but should be charged for the full calendar period elapsing between shipment to and from the job. It also provides that one-half of the first shift rate should be paid on second shift operations (Pltfs. Ex. 17-B, Appendix B, pp. 27-28, *infra*). The Bureau of Reclamation's

Equipment Rental Schedule is based on the Associated General Contractor's schedule, and is designed to provide reasonable rental rates for payment to contractors on cost plus work. It likewise contains monthly rental rates for one-shift operation and provides for payment of one-half the first shift rate for second shift operation (Pltfs. Ex. 17-C; pp. 181, 327, of Appendix C to Brief for the United States).[8] As in the case of the A. G. C. monthly rate, the Bureau's monthly rates are paid for the full calendar period that the equipment is assigned to the job without deduction for the time that the equipment is idle due to weather, repairs or Sundays (App. C, pp. 331-333, 352, 355-357).

The method followed by the contracting officer in reducing the Bureau's monthly rental rates to hourly rates was to divide the monthly rate by 30 to get a daily shift rate for first shift operation, add one-half of the first shift daily rate for second shift operation, and divide this total by the 16 hours in a two-shift day to get an hourly rate (Pltfs. Ex. 17, pp. 70-77, Defts. Exs. 17-V, 17-W; App. C, pp. 96-98, 327, 331, 344). It is obvious that such an hourly rate when applied to hours of actual operation makes no allowance for the time that the equipment was idle due to weather and repairs and that it would not yield the monthly rate unless the equipment worked 16 hours a day, 30 days a month (App. C, pp. 98-99).

In the appeal to the head of the department, the contractor pointed out that the contracting officer's method of reducing the monthly rates to hourly rates automatically deprived the contractor of the allowance for idle time which he would receive under the monthly rate (Pltfs. Ex. D, pp. 56-57). The appeal also showed in detail the method used by the contracting officer in computing his hourly rental rates (Id., pp. 59-66). The contracting officer's decision itself advised that the hours to which the hourly rates were applied

[8] Appendix C to the Brief for the United States consists of the pertinent portions of the testimony in this case, and will hereinafter be cited as "App. C".

were hours of operation (Pltfs. Ex. C, pp. 47, 50, 282). In addition, the department head was furnished by the contracting officer with a copy of the Associated General Contractor's schedule and was advised that it contained the fundamentals on which the rates in the Bureau's schedule were based (Defts. Ex. 17-V).

The department head then handed down his findings and decision in which he stated that the equipment rental rates used by the contracting officer were those set out in the Bureau's schedule, and that the rates in the Bureau's schedule were based on the Associated General Contractor's schedule, and take into account idle time (App. B to Brief for United States, pp. 46-47).

It is quite true that the monthly rates in the Bureau's schedule and the Associated General Contractor's schedule make an allowance for idle time and are paid for the full calendar period without deduction for the time that the equipment is idle due to weather, repairs and Sundays. The department head's decision simply ignored the real complaint which was that the contracting officer reduced these monthly rates to hourly rates by a method which obviously made no allowance for idle time whatsoever when applied to hours of actual operation. The only explanation of such a decision is that he consciously approved an hourly rental rate arrived at by a method which he knew was unfair, or that he was indifferent to what the dispute was about. In the one case he would be guilty of bad faith or failure to exercise an honest judgment; in the other of error or negligence so gross as necessarily to imply bad faith.

The same is true with respect to his decision approving the contracting officer's hourly rates for maintenance of equipment. Here, the proof shows:

The hourly rates for field repairs and maintenance used by the contracting officer in his adjustment under Order for Changes No. 3 were not based on costs on respondents' job (App. C, p. 358). They represented only a small fraction of respondents' actual cost of maintenance and field

repairs on this job.[9] While the subordinates who prepared the hourly rates for maintenance and field repairs used by the contracting officer in making his adjustment testified that such rates were based upon the costs of the Bureau and certain other governmental agencies, they were unable to give any details or explain just how they arrived at such hourly rates. While one of them was requested to furnish the Court the data he was supposed to have considered in arriving at such hourly rates, he never did so nor did the Government ever account for his failure to do so (App. C, pp. 327, 328, 333, 346, 354, 355). On the other hand, the explanation of these rates which the contracting officer furnished to the contractor shows on its face that such rates did not purport to be based on costs on any job, but were described as "assumed" or were merely percentages of his hourly rental rates which themselves were grossly unfair (Defts. Ex. 17-W). The only maintenance rate which purported to be based on another job was that for the jackhammer, described as the approved rate on Shasta Dam. On the jackhammer, having a capital value of $205, the contracting officer allowed a maintenance rate of 20 cents per hour compared to only 23 cents per hour on a RD8 caterpillar tractor having a capital value of $7905, and only 30 cents per hour on a Lima Dragline having a capital value of $39,189 (Defts. Ex. 17-W).

In the appeal to the head of the department the contractor complained that the contracting officer's figures for maintenance were far below the actual cost of maintenance and pointed out that high maintenance costs were experienced in operating in these cobble materials (Pltfs. Ex. D, pp. 51-55, 57, 58). Attached to the appeal as Exhibit Y

[9] Respondents introduced evidence of the actual cost of field repairs and maintenance during the 1940 season when the work in question was performed, and divided such costs by hours of operation to obtain the hourly cost (Pltfs. Ex. 17-D; App. C, pp. 80-92). Although during the trial of this case the Government auditor checked respondents' cost records at their office he was never called as a witness (App. C, p. 536).

was the above-mentioned explanation of the contracting officer's maintenance rates which he had given to the contractor (Id., pp. 59-66).

In his decision on appeal the department head approved the maintenance rates used by the contracting officer, stating that they were determined on the basic of experience of the Bureau and other governmental agencies (App. B to Brief for the United States, p. 48). No attempt was made to check the actual costs of maintenance on the job although paragraph 8 of the specifications gave the Government the right to do so (App. A, *infra*, pp. 24-25). As stated before, the department head had before him the contracting officer's letter explaining to the contractor the basis of the hourly rates for maintenance used in the adjustment. This explanation showed on its face that these rates were not based on any job but were assumed and were fixed percentages of hourly rental rates which the department head knew or should have known were themselves grossly unfair.

In view of the above respondents submit that the proof would support a finding that the findings and decision of the head of the department approving the hourly rental rates and hourly maintenance rates used in the contracting officer's adjustment were not in good faith, or were not the exercise of an honest judgment, or were so grossly erroneous or negligent as necessarily to imply bad faith. Under these circumstances, if this Court should hold that the Court below was not justified in setting aside the decision of the head of the department on the basis of a finding that the methods of computation used by him were arbitrary and capricious, the case should be remanded to the Court of Claims with instructions for a more explicit finding on the subject of good faith. As stated *supra*, pp. 15-16, this was done in the *Ripley* case, although the pleadings in that case did not allege bad faith or gross error.

Petitioner seeks to give some rational basis for the equipment rental rates used in the adjustment under Order for Changes No. 3 by pointing out that the Associated General

Contractor's schedule itself indicates that it is not an inflexible tariff and that its rates should be applied in the light of experience. Petitioner then contends that because the equipment was constantly shifting back and forth between the work under Order for Changes No. 3, and other items of work, it was therefore reasonable for the contracting officer and the head of the department to assume that the contract unit prices for the other items of work provided adequate compensation for any time that the equipment was idle. Thus, asserts petitioner, the inclusion of an idle time factor for additional work not contemplated in the original contract would necessarily result in duplication.

This contention is without merit. There is nothing in the record which remotely indicates that the contracting officer, the department head, or any one else ever took into account any such theory as a justification for the method by which they reduced their monthly rates to hourly rates. Moreover, even if they had relied on any such theory they would have been completely unjustified in doing so. In the first place, if it be assumed that the Associated General Contractor's schedule is intended only as a guide, nevertheless the Bureau itself has prepared its own schedule of rates, based on the Associated General Contractor's schedule. All field offices of the Bureau are required to and do use the rates in the Bureau's schedule in preparing extra work orders on a cost plus basis (Pltfs. Ex. 17-C, App. C, pp. 325, 330, 331, 340).

In the second place, the Government, asserting that it is reasonable to assume that the contract unit prices paid for other items of the contract work provided adequate compensation for idle time for the equipment, would have these contract unit prices absorb all the idle time of the equipment whether it occurred during times that the equipment was assigned to work covered by these contract unit prices or during times when it was assigned to the cost plus work covered by the Order for Changes No. 3. Thus,

under defendant's theory, none of the idle time customarily paid for under the Bureau's own monthly rental rates would be allowed in Order for Changes No. 3. This is manifestly unfair as some equitable share of the allowance for idle time should be credited to this cost-plus work. What the Court of Claims has done is to arrive at an hourly rental rate which, when applied to hours of actual operation, makes allowance for the idle time customarily paid for in the monthly rate. Such hourly rental rate was then applied only to hours of actual operation on the work covered by Order for Changes No. 3 (R. 127-129). It is, therefore, clear that no duplication of payment for idle time is involved. No duplication would occur unless such hourly rental rate had been applied not only to the hours of operation under Order for Changes No. 3, but also to the hours of operation on the other work to which the contract unit prices were applicable.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below should be affirmed.

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OCTOBER, 1961.

APPENDIX A

Article 3 of the contract provides:

Changes.—The contracting officer may at any time, by a written order, and without notice to the sureties, make changes in the drawings and/or specifications of this contract and within the general scope thereof. If such changes cause an increase or decrease in the amount due under this contract, or in the time required for its performance, an equitable adjustment shall be made and the contract shall be modified in writing accordingly. No change involving an estimated increase or decrease of more than Five Hundred Dollars shall be ordered unless approved in writing by the head of the department or his duly authorized representative. Any claim for adjustment under this article must be asserted within 10 days from the date the change is ordered: *Provided, however,* That the contracting officer, if he determines that the facts justify such action, may receive and consider, and with the approval of the head of the department, or his duly authorized representative, adjust any such claim asserted at any time prior to the date of final settlement of the contract. If the parties fail to agree upon the adjustment to be made the dispute shall be determined as provided in article 15 hereof. But nothing provided in this article shall excuse the contractor from proceeding with the prosecution of the work so changed.

Article 15 of the contract provides:

Disputes.—Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the contracting officer subject to written appeal by the contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties thereof. In the meantime the contractor shall diligently proceed with the work as directed.

Paragraph 8 of the specifications provides:

8. *Data to be furnished by contractor.*—The contracting officer, through his authorized agents, shall have

access to all pay rolls, records of personnel, invoices of materials, and any and all other data relevant to the performance of the contract or necessary to determine its cost, and the contractor shall furnish at the end of each month an itemized statement in a form satisfactory to the contracting officer of the cost of all work under the contract.

APPENDIX B

The Schedule of Contractors Ownership Expense, issued by the Associated General Contractors of America (Plfts. Ex. 17-B), provides in part:

FOREWORD.

* * * *

The general plan of presentation is the same as the last previous edition which made its appearance in 1930. The items of equipment ownership expense are expressed as a percentage of the original capital investment. Every endeavor has been made to gather authentic information as to cost experience. The percentage rates set up for the various items represent an approximate average of conditions under which the equipment has been operated.

The percentage rates are subject to adjustment to fit the experience of the individual contractor. It is intended that this schedule prove useful as a basis or guide, but it is recognized that individual experience may vary from the average within a fairly broad bracket. Some of the factors justifying adjustment of the rates shown are: weather conditions—where the equipment is located—whether in the south where the construction season is long as contrasted with the relatively short season of the north; exposure of the equipment, i.e., the relative rigor of the work at hand; care of the equipment, both in operation and maintenance.

The A. G. C. schedule ends with the development of average annual cost expressed as a percentage of capi-

tal investment. From this a monthly use rate is developed, also expressed in percentage of capital investment.

In order to make the schedule as useful as possible, a price representing the original cost of standard high grade equipment is given. To demonstrate the operation of the schedule, the calculated per cent per month has been applied to the price given, and a cost per month expressed in dollars has been calculated.

In using this schedule it should be remembered that it contains no element of profit or return sufficient to justify continuous reinvestment in construction equipment for rental to others. The rates shown will not ordinarily be rates on which a concern engaged in renting equipment could exist. A contracting firm desiring to rent its equipment would need to add a ready-to-serve charge to cover overhead in addition to a profit.

* * * * *

EXPLANATION OF ITEMS OF EQUIPMENT OWNERSHIP EXPENSE. CONTRACTORS' ANNUAL EQUIPMENT EXPENSE.

Annual equipment as treated in the accompanying schedule embraces those items that are more or less constant and cannot ordinarily be determined accurately for a specific project. It does not include loading, shipping, erecting, operating or dismantling, nor does it include fuel, lubricates, supplies, wages or transportation of operating crews or any of the contractor's general expense of doing business. Minor or field repairs are not included because they are generally regarded as job or operating costs that require special study for each project, and because they are generally carried as a cost of the work on cost plus a fee operations. The annual equipment expense is composed of but six items, which are as follows: (1) Depreciation, (2) Major Repairs and Overhauling, (3) Interest on the Investment, (4) Storage, Incidentals

and Equipment Overhead, (5) Insurance and (6) Taxes.

These six items are expressed as percentages of the capital investment, and the capital investment is considered as the original cost of the machine f.o.b. factory or point of shipment, plus the expense of freight to the contractor's initial unloading or receiving point, plus the cost of assembling, testing and making ready for use. Any similar expenses incurred after the initial set-up are not included in the investment.

* * * *

Major Repairs and Overhauling.

Major or shop repairs include those items of heavy repair which usually keep a machine idle for an extended period in contrast with minor or field repairs which entail comparatively little delay and which are necessary to keep the machine in operation. Such repairs include overhauling and painting at the contractor's shop or yard, but do not include rebuilding.

* * * *

Monthly Equipment Expense.

The annual equipment expense explained in the preceding paragraphs must be recovered by a contractor from work that he performs. To do this it is necessary to establish for each item a monthly charge of such amount that when multiplied by the average number of working months it will yield a revenue equal to the annual expense. In other words, the monthly charge for any item equals the annual expense divided by the average number of months during which the machine is in use. It varies extremely, depending on the type of equipment, the climate, nature of the work, business conditions and other factors.

The average number of working months for each item of the schedule is based on average climatic conditions for the nation as a whole, such as usually prevail